
CABLE LANGENBACH KINERK & BAUER LLP MEMORANDUM

To: Branda Andrade, Assistant General Counsel

From: Colleen Kinerk

Subject: Report on Whistleblower Complaint

Date: Friday, May 29, 2015

I. Introduction

This Report addresses the Whistleblower Complaint (“Complaint”) tendered to Snohomish County Public District Commissioner Kathleen Vaughn on March 17, 2015.

The author of the Whistleblower Complaint is entitled to anonymity and will be referred to in this Report as “the W.B.” The Complaint is not attached because the identity of its author would be evident from the face of the document.

The Complaint focuses on a series of contracts between Snohomish County Public Utility District No. 1 (“Sno PUD” or the “District”) and 1 Energy Systems (“1 Energy”). The contracts are referred to, respectively, as Professional Services Contract #64081, Mesa I (A.&B.), Mesa II and two software contracts (“DERO” and “BPA”). Mesa III is a pending contract proposal still under consideration by the Commission.

All of the Contracts fall within the purview of the Utility’s “Smart Grid”. Reduced to basics, the contracts called for the design and installation of battery operated power storage modules at two different utility substations and creation of related software. The Contracts were to provide the foundational basis for the Utility to develop better ways to use its electric grid.

The W.B. raised concerns that fall into the following categories:

- Whether the Utility complied with its policies and state laws in awarding contracts to 1 Energy without a competitive procurement process.
- Whether potential or actual conflicts of interest arose with respect to any of the contracts and if so, whether any such conflicts were fully and timely identified and addressed.
- Whether any personal financial benefit accrued to any Sno PUD employee as the result of awarding one or more of the referenced contracts to 1 Energy.

The W.B. raised other specific concerns that fall under the umbrella of these categories. They are also addressed in the Report.

II. Summary Overview of the Investigation

It is necessary to read the Report in its entirety to understand the conclusions reached by this Investigator. Based on this Investigator's review of voluminous documents and interviews with the witnesses identified below, this Investigator made the following findings.

- The Utility followed its policies and the law with respect to each of the contracts between the Utility and 1 Energy, with one exception. With respect to the initial contract, PSC #64081, neither the Utility nor its then employee, David Kaplan, satisfied in full the obligations imposed by the Utility's policy set forth in Directive 90, which prohibits conduct that gives rise to the appearance of a conflict of interest.
- This Investigator found no evidence to support the allegation that Mr. Steve Klein, the Utility's former CEO, sought or received an offer of employment or any other financial benefit from 1 Energy. Similarly, this Investigator found no evidence

that any other Utility employee sought or received an offer of employment or any other financial benefit from 1 Energy.

- The Report also sites to a potentially unresolved issue between 1 Energy and the State Department of Commerce relating to the Utility's application for a Clean Energy Fund Grant.

III. Witnesses Interview and Documents Received by the Investigator

The Investigator interviewed the following witnesses:

1. The W.B.;
2. Mr. Steve Klein (retired) CEO of the Utility;
3. Mr. Dave Kaplan (former Utility employee and CEO of 1 Energy)¹;
4. Ms. Anne Spangler (General Counsel and current interim CEO of the Utility);
5. Mr. Will Odell, Lead Smart Grid Program Manager;
6. Mr. Craig Collar, Assistant General Manager, Power Rates and Transmission Management Division;
7. Mr. Chris Heimgartner, Assistant General Manager, Distribution and Engioneering Services.

Each of the witnesses voluntarily appeared for his/her interview and cooperated with the Investigator. The Investigator was provided with voluminous documents including but not limited to policies, contracts, grant documents and related emails. The sources for the referenced documents include the Utility, the W.B. and the witnesses.

¹ Mr. Kaplan required that his interview be conducted in the presence of Mr. Tom Melling, the Executive Vice President of Operations and General Counsel for 1 Energy.

These documents have been compiled and are being retained at the office of the Investigator.

IV. Overview of the Sno PUD Contracts with 1 Energy

The Chart set forth below identifies each of the contracts between Sno PUD and 1 Energy including the dates executed, the dollar amount of the contract and the dollar amounts of grant funding secured by the Utility to help defray costs.

Contract #	64081	70241	79931	81171	82014	Total
Approved by Commission	09/06/2011	11/06/2012	10/06/2014	01/20/2015	03/03/2015	
Contract Date	09/08/2012	11/20/2012	10/06/2014	01/21/2015	03/17/2015	
Original Amount	\$800,000	\$3,500,000	\$8,792,000	\$1,471,000	\$1,686,887	\$16,249,887
Amended Amount		\$4,306,845				
Description	Energy Storage System Field Test Project	Mesa Appliance Prototype ESS	Mesa 2 Energy Storage system - Everett Substation	Energy Storage Optimization - DERO Project	Energy optimization	
Grant Funding		\$2,400,000	\$4,400,000	\$500,000	\$2,000,000	\$9,300,000

The Chart does not include the proposed Mesa III contract for \$4,026,360 because it has not been executed and remains under consideration by the Commission.

V. Sno PUD's Protocols for Contract Consideration, Review and Approval

The contracts with 1 Energy required approval by the Board of Commissioners. Many steps occur before contracts are presented to the Commission for its decision to approve or not. Sno PUD contends that in each instance, it followed the internal protocols and published policies for evaluating, negotiating, drafting and reviewing of contracts, and that it did so with the assistance of the Legal Department. Given the nature and scope of the projects, several utility personnel were involved in the underlying assessment of the proposed projects.

With the exception of one software contract (DERO), all of the contracts between Sno PUD and 1 Energy for professional services were procured without a competitive

process. In each instance, Utility personnel conducted due diligence to justify waiver of the competitive procurement process.² As the Report will discuss in more detail, the record made available to the Investigator documented sufficient grounds to justify waiver of a competitive procurement process in the Utility's contracts with 1 Energy, with the exception of the first contract, PSC #64081.

Detailed technical and financial information was made available to the Commissioners to inform their deliberations and decision making concerning the contracts with 1 Energy. The briefing process included submission of documents and substantive presentations by the Utility personnel who had helped evaluate and develop the various projects to which the contracts relate.

**VI. Sno PUD's Strategic Plan and Decision to Invest
Some Financial Resources in Technology and Product Innovation**

The allegations in the Complaint must be analyzed within the larger context of the Utility's operations, anticipated future needs and its Strategic Plan.

Formed in 1936, Sno PUD is a consumer owed electrical utility that serves over 330,000 electrical customers and many thousands of water customers. It is one of the largest public utilities in the United States and the second largest in Washington State. It encompasses nearly 2,200 square miles. Its operations are vital to the residents of the geographic area that it serves.

The Utility's operations do not take place in a vacuum. Sno PUD is part of a larger, complex electrical power grid. Sno PUD annually acquires approximately 80% of its power from the Bonneville Power Administration (the "BPA"), the operator of the grid.

² The Utility has entered into other contracts with other suppliers/providers that were not procured through a competitive process. It is not uncommon at the Utility.

Sno PUD had the option to sit back, continue to purchase energy from BPA and provide it to utility customers. However, the Utility and its Board of Commissioners viewed the preservation of the status quo as a less than optimal approach to planning for the future.

A Strategic Plan for the Utility was developed with input from Utility employees, executives and the Commissioners. The Strategic Plan reflects the Utility's response to the effects of climate change and the national, state and regional imperatives to pursue conservation, sustainability and renewable energy sources.

As the Strategic Plan evolved, it was decided that some of the Utility's financial resources would be allocated to experiment with innovative prototypes in a field test setting. It was also anticipated that the Utility would seek funding through grants to help mitigate the costs. This provides a backdrop for addressing the series of contracts with 1 Energy which have elicited the pending Complaint.

VII. Battery Storage Emerges as a Priority for Sno PUD - 2010

Like utilities across the nation, Sno PUD has found it necessary to grow and diversify its portfolio of power resources in order to best respond to the current and projected future needs of its customers. Sno PUD has committed to meet all future growth needs with conservation and a diverse mix of renewable resource technologies. Energy storage fits naturally with these objectives.

Battery storage technology was identified by Sno PUD as a priority directive starting in approximately 2010. Although still a nascent field, energy storage offered promise of tangible benefits. A battery storage system would increase flexibility on the

power grid, reduce peak load and help balance intermittent renewable energy resources like solar and wind.

When successfully implemented, energy storage can reduce line congestion and transmission losses. It can minimize the need to run expensive power plants and to spill renewable energy during times of excess energy supply. When the utility load is high and market prices are steep, the Utility can draw from its battery storage resources to minimize its purchases. In some circumstances, energy storage might offer the Utility a revenue source because of the ability to sell surplus energy to other users and/or to store energy for other users.

VIII. The Interface Between the Utility's Need for Technological and Product Innovation and For-Profit Suppliers/Vendors

The Whistleblower Complaint reveals some of the difficult issues that arise when a utility makes the decision to invest personnel and financial resources to acquire new green energy technology and products in order to achieve conservation and sustainability goals. There is an inevitable economic interface between the Utility's future energy needs, the Utility's commitment to conservation and sustainability, its use of personnel and financial resources to accomplish these objectives (augmented by state and federal funds) and the role of for-profit businesses that provide such technology and products to utilities.

Public-private partnerships are essential to the development of new green energy technology and products. The participants in these joint undertakings are motivated by some shared and complimentary objectives like conservation and sustainability. But it is not entirely altruistic. There is a significant commercial objective that is the predominant driver for the for-profit business.

This financial/economic component is reflected in the criteria established by the State Department of Commerce for Clean Energy Fund grant applications. The Department of Commerce was explicit about its intent to invest in green energy products and technology in order to help the environment and to create new jobs and businesses in this State.

IX. The Relationship Between Mr. David Kaplan and Sno PUD

Mr. David Kaplan is a former, short-term employee of Sno PUD (February 1, 2010 through July 29, 2011) and the founder and CEO of 1 Energy. He has been a figure in State clean energy circles for many years. After a successful career at Microsoft, Mr. Kaplan started a company called V-2 Green. V-2 Green delivered the first technology platform for connecting electrical cars to the power grid. It was sold in 2008.

Mr. Kaplan is a distinguished Visiting Professor at the University of Washington in the Department of Electrical Engineering and Computer Science. Of significance to this Report is the fact that Mr. Kaplan also served as a consultant to the Washington State Department of Commerce from April 2009-January 2010.

David Kaplan and Steve Klein became acquainted through their involvement with the Washington State Clean Technology Alliance. They shared a mutual fascination with technology, innovation and clean energy. They also lived in close proximity and would periodically take walks together during which they discussed these shared interests.

In late 2009-early 2010, Mr. Klein invited Mr. Kaplan to tour Sno PUD's facilities. Mr. Craig Collar, an Assistant General Manager of the Utility, served as a guide during Mr. Kaplan's visit. Mr. Kaplan expressed to Mr. Klein and to Mr. Craig Collar his desire to learn about the Utility from the inside.

Having very recently concluded his work as a consultant for the State Department of Commerce, Mr. Kaplan was in search of a new opportunity. He lacked hands on experience with the operations of a utility; a deficit he wanted to address. Discussions ensued between the parties. A decision was reached to invite Mr. Kaplan to join the Utility. The District determined that Mr. Kaplan should be hired as an employee rather than retained as a consultant.

Mr. Kaplan accepted a position as a time limited employee reporting directly to Steve Klein. He had no subordinates. His salary was \$193,440 per year. According to Mr. Kaplan, Mr. Klein gave him flexibility in terms of working hours and also agreed that he could continue consulting for outside clients, provided these matters were not in conflict with his work for the Utility.

Mr. Kaplan's initial focus was to assess the IT needs of the Utility and to devise a plan for improvement in the design and delivery of IT services. The Utility was beset with a multiplicity of software programs and a myriad of licenses. Since Mr. Kaplan had acquired valuable expertise in this field during his tenure at Microsoft, the Utility concluded that he could help identify some solutions.

At Mr. Kaplan's direction, a Business Architecture Board ("BAB") was assembled. Its members were comprised of IT users across the organization. Mr. Kaplan was also involved in identifying possible candidates to serve as the Chief Information Officer. By all accounts, Mr. Kaplan's led a successful effort to upgrade the Utility's IT structure and operations.

From the start, Mr. Kaplan had direct access to Mr. Klein and other senior executives of the organization. Mr. Kaplan regularly attended leadership committee

meetings with Mr. Klein and other Utility executives. His work in the IT arena brought him into frequent contact with numerous employees who were deployed across the Utility's operations.

Mr. Kaplan and Mr. Klein were very open about the fact that the arrangement would be temporary. Mr. Kaplan made clear to Mr. Klein, and later to other senior level executives of the Utility, that he intended to identify an entrepreneurial opportunity in the course of his work for the Utility.

Mr. Klein and Mr. Kaplan continued to confer regularly about technology and product innovation. Their discussions focused increasingly on battery storage which had emerged as an option of interest to the Utility. Eventually, other members of the Utility's leadership team participated in this ongoing dialogue about the potential for deployment of battery power storage.

In his capacity as an employee of the Utility, Mr. Kaplan was paid to attend conferences dealing with energy storage and to research the subject. This work was directly beneficial to the Utility but it also helped Mr. Kaplan to develop and refine his business plan for 1 Energy.

By the summer of 2011, Mr. Kaplan became directly involved in discussions with Mr. Klein and other senior level leaders of the Utility about a possible project following his departure. These discussions included face-to-face meetings and email exchanges. Material components of a future contract were explored in depth by the Utility and Mr. Kaplan prior to Mr. Kaplan's departure from the Utility on July 29, 2011.

X. Professional Services Contract No. PSC # 64081

Sno PUD entered into professional services contract PSC #64081 with 1 Energy in September, 2011. The contract amount was \$800,000. At this point, Mr. Kaplan was the owner and sole employee of 1 Energy. The company had been created by Mr. Kaplan in 2010 when he was contemplating a different undertaking. 1 Energy had sat dormant until it was activated for the professional services contract with Sno PUD.

PSC #64081 was approved by the Board of Commissioners at a meeting that occurred on September 16, 2011. It was presented on the consent agenda along with several other contracts. The consent agenda is a vehicle used by the Contracts and Purchasing Department to present a variety of contracts to the Board. There is an individual fact sheet submitted for each proposed contract. The Commissioners are provided the opportunity to ask questions or seek clarification.

A Competitive Waiver Exception form had been prepared to justify the Utility's decision to not use a competitive procurement process on PSC #64081. The waiver cited several factors including the nascent nature of energy storage and 1 Energy's deep familiarity with Sno PUD's operations.

The negotiations also resulted in 1 Energy reserving ownership of the intellectual property developed in the course of the contract. That would continue to be a material term for 1 Energy in its future contracts with the Utility.

Once the contract was executed, Mr. Kaplan proceeded to hire employees for 1 Energy, including a member of his immediate family. Ultimately, PSC #64081 would be superseded by another larger contract that would be referred to as Mesa I. At the time the

Mesa I contract was executed, approximately one-half of the funds for contract PSC #64081 (\$400,000) had been expended.

XI. The Cancellation of PSC #64081 and Execution of Mesa I

The following developments caused Sno PUD and 1 Energy to transform the project as originally envisioned in PSC #64081 and to enter into a new contract for an expanded and costlier endeavor (Mesa I). The price tag for Mesa I was \$3.5 million (later increased to \$4.3 million).

First, the Electric Power Research Institute (“EPRI”) did not select the Utility to host an energy storage system as had been contemplated by PSC #64081.

Second, the contract had required that an energy storage system (“ESS”) integrator be selected to integrate the various system components. Efforts to locate and persuade potential industry candidates had been unsuccessful.

Third, as a result of 1 Energy’s research, it was determined that there were no open, non-proprietary communications standards for connecting the ESS components with software.

Finally, none of the existing suppliers were apparently willing to put their proprietary communication technology into the public domain to enable development of an open standard.

In hindsight, it appears that the scope of work described in PSC #64081 was ambitious and predicated on certain beliefs and assumptions about what would be entailed in building, installing and testing a battery operated power storage prototype. However, the work did yield a more informed assessment of the costs and logistics that would be required to design, construct and install the desired end product. The monies

expended pursuant to contract PSC #64081 accelerated the learning curve about energy storage for Sno PUD as well as 1 Energy and its CEO. It also led to a series of contracts with 1 Energy that grew in scope and cost, albeit with the influx of substantial grant monies.

XII. Development and Adoption of the Mesa Standards

The contracts between the Utility and 1 Energy, as well as the Utility's Application for a State Clean Energy Fund grant, are replete with references to the Mesa Standards. The story behind the Mesa Standards is integral to understanding the circumstances surrounding the Mesa I, II and III contracts.

From very early on, Dave Kaplan, CEO of 1 Energy and Steve Klein, CEO of Sno PUD were intent on effectuating changes on a national scale in order to have Sno PUD and other utilities positioned to require that suppliers for the components of energy storage systems adopt uniform standards. The so-called Mesa Standards reflected their desire, and that of other stakeholders, to have standard electrical and communication interfaces to connect batteries, power converters and software components into modular energy storage systems. The objective was to have "plug and play" energy storage capabilities readily available in the marketplace.

The concept was innovative. If adopted widely, it would be of direct benefit to Sno PUD and other utilities since it would serve to lower costs. It would also help 1 Energy to position itself in the lucrative green energy market to sell its software and professional services to other utilities. 1 Energy, the architect of the software for the Mesa I and Mesa II projects, also stood to benefit from the branding opportunity that arose from having the name "Mesa" attached to the standards.

Mr. Klein and Mr. Kaplan actively and publicly advocated for adoption of the Mesa Standards within their spheres of influence among utilities, state government, state universities and the private sector. They helped form the Mesa Alliance and solicited participation from other utilities. According to its proponents, the Mesa Standards would on an industry-wide basis, accelerate interoperability, scalability, safety, quality, availability and affordability of energy storage components and systems.

The Mesa Alliance was launched in Washington State. It was subsequently incorporated as a not for profit entity in California in 2014. This was an intentional step. The utilities in California had been legislatively mandated to achieve energy storage goals pursuant to specific deadlines. As well, California represented a vast market with a huge potential for selling energy storage products and related software.

The Mesa Standards exemplified the confluence of public benefit and entrepreneurial gain that is a hallmark of the joint ventures between utilities and for-profit businesses seeking innovation in green technology and products.

XIII. Current Status of the Contracts with 1 Energy

Each of the Mesa contracts, as well as the software contracts, set forth a schedule of deliverables, with specific milestones that need to be reached as a condition precedent to issuance of each installment payment. Utility personnel have confirmed that the contracts are tracking the milestones, that the delays have been relatively short and that they are optimistic the projects will be successfully completed and implemented.

The W.B. raised a concern about the fact that the Utility has made some direct payments to subcontractors involved with the projects. The Utility states that those

situations have been infrequent and routinely involved a specific, tangible deliverable received from the subcontractor.

The software contracts (BPA and DERO) are still in the early stages of development.

XIV. Brief Description: Mesa I - (\$3.5 Million - later \$4.3 Million)

The Mesa I project is situated at a power station near the Utility's Operations Center (Hardeson). It is a hybrid of personal services and equipment. The contract calls for the design, construction and installation of a battery storage power unit using lithium/ion batteries. It is a prototype project. Mitsubishi and LG Chem are the battery suppliers. Parker Hannifin is the power conversion system provider. 1 Energy serves as the systems integrator and software designer.

XV. Brief Description: Mesa II - \$8.7 Million

This is a second prototype project where the PUD will install a power storage unit using vanadium batteries at a second utility substation in Everett. The contract is a hybrid of personal services and equipment. (Vanadium batteries were not available at the time of Mesa I.) Each type of battery has distinctive properties. Vanadium batteries are noted for being longer lasting. The project is intended to also allow for integration of intermittent wind power.

The power storage system is to be built by UniEnergy Technologies LLC ("UniEnergy"). UniEnergy was created in 2012 and is located in Mukilteo, Washington. The company agreed to manufacture the system to the Mesa Standards.

Parker Hannifin was selected to provide the power conversion system for Mesa II. 1 Energy serves as the systems integrator and software designer.

XVI. The Selection of 1 Energy to Serve as Systems Integrator

As noted, on both Mesa I and Mesa II, 1 Energy serves as the integrator of the components, in addition to procuring them on the open market, and writing proprietary software. 1 Energy did not seek the role of systems integrator. Sno PUD pressed 1 Energy to take on that role for several reasons. First, the Utility decided to offload potential liability by having a single contractor. Second, the Utility did not believe that it possessed the requisite internal expertise to serve as its own systems integrator. However at the time 1 Energy was asked and agreed to take on the role of systems integrator, it had not previously served in that capacity.

XVII. Brief Description: Software Contract: BPA

Sno PUD acquires most of its energy from BPA. The software is intended to facilitate the communications between the two in order to promote efficiency, flexibility and to achieve reductions in cost for the Utility.

XVIII. Brief Description: Software Contract: DERO/Optimizer

The DERO (Optimizer) software is intended to enable the Utility to implement fleet management of its energy assets. The contract was executed in January 2015.

This software contract represented the single instance in which 1 Energy was required to participate in a competitive procurement process. OATI, 1 Energy and one other potential vendor were invited to make presentations to the Utility.

Part of the internal discernment process involved the convening of the Utility's Energy Storage Steering Committee to address the relative merits of the proposals. There were different opinions voiced at the Committee meeting where the pros and cons of the competing proposals were debated.

The Utility's Assistant General Managers endorsed 1 Energy's proposal. One Committee member felt that the Assistant General Managers were too assertive on behalf of 1 Energy.

The Steering Committee is a soundboard and not intended to operate as a democratic body. It provides a valuable platform for the exchange of professional opinions on important matters for the Utility. The ultimate decision whether or not to approve the contract was to be made by the Commission. Depending on the circumstances, and in the absence of a consensus by the Steering Committee, the advocacy of the Assistant General Managers could be viewed by some as favoritism. That inference is more likely to manifest where, as here, the Utility has executed a series of valuable contracts with the same vendor.

XIX. Legal Analysis - Avoiding an Actual Conflict of Interest or the Appearance of a Conflict

A. The Negotiation for and Execution of PSC #64081.

Based on the record available to the Investigator, the initial contract between 1 Energy and the Utility was executed without proper regard of Utility policies about actual conflicts of interest or the appearance of the same.

Pertinent excerpts from Sno PUD Policy, Directive 90 are set forth below:

Expectations - Conflict of Interest. District employees may not pursue personal business interest/activities, which are in conflict with the District's interests. Employees must disclose any potential or actual conflict of interest situations and discuss these situations with their immediate supervisor.

Responsibility - Conflict of Interest. Employees and their supervisors must take measures to prevent either actual conflicts or the appearance of conflicts of interest and to

ensure that such situations are resolved consistently with this Directive.

Mr. Klein and other senior level Utility executives were enthusiastic about the benefits that would ensue from a successful energy storage project. This represented a cutting edge innovation directly tied to the Utility's green energy goals. They had tremendous confidence in their colleague, David Kaplan.

That enthusiasm should have been better tempered and more sensitivity demonstrated regarding the potential for a conflict of interest, or the appearance of a conflict of interest.

PSC #64081 was a research and development project which was an uncommon undertaking for the Utility. Partnering with a for-profit entity to explore the design and construction of an experimental prototype energy storage system was not an ordinary event. It warranted careful consideration of and adherence to the Utility's policies and protocols.

Directive 90 requires the particular District employee and potential contractor to disclose all material and pertinent information that bears upon the issue of either an actual or apparent conflict of interest. Directive 90 also requires the supervisor(s) of the employee in question to take measures to prevent the creation of either an actual conflict or the appearance of a conflict of interest. For the reasons set forth below, the Investigator finds that neither the Utility nor David Kaplan met their obligations under Directive 90.

David Kaplan came to the Utility for the express purpose of identifying a business opportunity. During his tenure at the utility, David Kaplan's work included research relating to energy storage. Well before the conclusion of David Kaplan's employment

with the Utility, he was refining a business plan that related to energy storage. In the summer of 2011, David Kaplan actively sought a contract with the Utility relating to energy storage that would become effective in near seamless fashion after his departure.³

Mr. Kaplan brought skills of considerable value to the Utility. In exchange, Mr. Kaplan was allowed to educate himself about the Utility's operations and the subject matter of battery power storage to serve a dual agenda. That unique and valuable learning opportunity greatly benefitted Mr. Kaplan. Thereafter, Mr. Kaplan sought to parlay that learning opportunity and his contacts with the Utility's CEO and some senior executives, for his own financial gain.

Certainly, a mutual exchange of benefits often arises in employer/employee relationships. And a former employee can subsequently contract with a former employer either in the private sector or the public sector. Mr. Kaplan was not required to scrub his brain of the knowledge he had acquired at the Utility, but he was subject to the conflict of interest rules during his tenure there.

As discussions for the contract proceeded, Mr. Kaplan continued to work side by side with the same executives who would ultimately advocate to the Commission that it approve the contract with his company, 1 Energy. And his work for the Utility related directly to the subject matter of the contract.

Mr. Kaplan identified for this Investigator the steps he took while still employed at Sno PUD to avoid any actual or potential conflict of interest. These steps included the use of a private email address and the clear communication that he was negotiating solely

³ On October 15, 2010, Mr. Kaplan filed a patent application with the United States Patent and Trademark Office (Pub. No. US 2001/0093127A1.) The Patent Application appears to relate in some way to the business plan that Mr. Kaplan was continuing to develop while employed at the Utility. The Provisional Application for the patent was filed by Mr. Kaplan on October 16, 2009, while he was still consulting for the State Department of Commerce.

for 1 Energy and that the Utility had its own arms-length negotiator. Under the circumstances, those steps fell short.

The same is true with respect to the Utility. There should have been more attention paid to Directive 90 given the unique circumstances of entering into a research and development contract with a soon to be former employee whose expertise had been acquired, in part, by the special access afforded him by the Utility. As Mr. Kaplan's supervisor, Mr. Klein should have been more vigilant in avoiding the appearance of a conflict.

B. Time Frame of the Negotiations

There was not a mandatory waiting period imposed on either the Utility or Mr. Kaplan before a post-employment contract could be entered into by the parties. However, it would have been prudent for the Utility to have imposed a time-out following the end of Mr. Kaplan's employment before negotiations for the contract commenced. This was not an imperative or emergent situation that required expedited contract negotiations. Moreover, Mr. Kaplan's business plan for 1 Energy strongly indicates that he would not have abandoned the opportunity to contract with the Utility had he been required either to defer negotiations while he was still employed at the Utility, or to participate in a competitive procurement process following his departure from the Utility.

C. Option for Independent Review of the Contract

Given the distinctive nature of the contractual undertaking, and Mr. Kaplan's recent employment at the Utility and unique access to insider information that gave him a competitive advantage, it would also have been advisable for the Utility to

arrange for an independent review of the contract. That could have been achieved by seeking guidance outside the Utility from a third party with the requisite expertise and no stake in the outcome.

D. Option to Use Competitive Procurement Process

Because PSC #64081 was a professional services contract, a competitive procurement process was not mandated. It was a matter within the Utility's discretion. However, a competitive procurement process is recommended by Directive 70 in some situations. As noted, the Utility did not routinely engage in research and development undertakings. For that reason, it was not the wisest or most appropriate course of action to forego a competitive procurement process with respect to PSC #64081.

The circumstances whereby Mr. Kaplan had attained his special and distinct knowledge of the Utility's operations and his role in formulating the Utility's plans to actively pursue energy storage conferred on him an advantage not available to other potential vendors. That was another factor that should have weighed in favor of a competitive procurement process. 1 Energy would very likely have been selected in a competitive procurement process and any inference of favoritism or undue influence would have been eliminated.

As noted earlier in the Report, justification was established for waiving a competitive procurement process on the other contracts between the Utility and 1 Energy.

E. Clean Energy Fund Grant Application to the State Department of Commerce.

Another aspect of the legal analysis pertains to the Utility's application for a State Clean Energy Fund grant for Mesa I (retroactively) and for Mesa II (prospectively).

The Utility's grant application was submitted to the Department of Commerce in December, 2013. Sno PUD was awarded a grant in the amount of \$7.3 million. The Grant Agreement between Sno PUD and the Department of Commerce was finalized in July 2014.

Sno PUD partnered with 1 Energy in the grant application process. By this time, 1 Energy had made a number of strategic hires. These included Mr. Daniel Malarkey who had served as the Deputy Director of the State Department of Commerce.⁴

Mr. Malarkey represented 1 Energy in the preparation of the Utility's Clean Energy Fund grant application submittal. Reportedly, Mr. Malarkey's involvement as a 1 Energy employee was openly shared with all parties, including the State. Certainly, the grant application clearly disclosed the active participation of 1 Energy in the projects for which funding was being requested.

Mr. Kaplan was asked about the implications of having Mr. Malarkey join 1 Energy and actively work on the Clean Energy Fund grant application in the wake of Mr. Malarkey's then recently concluded tenure with the Department of Commerce. Mr. Kaplan responded that 1 Energy had been verbally reassured by Mr. Malarkey that the latter had checked with his former employer and had been advised there was no problem.

The provisions of RCW 42.52.080 set forth the restrictions on the employment of a state officer or state employee after the termination of their employment with the State. RCW 42.52.080 identifies several possible scenarios in which a conflict will be deemed to arise and imposes time bars ranging from 12 to 24 months. The ultimate determination as to the applicability of RCW 42.52.080 and the related issue of compliance is a matter

⁴ 1 Energy also hired Mr. Rogers Weed who had served as the Director of the Washington State Department of Commerce under Governor Gregoire. Mr. Weed is the Vice President of Product Management of 1 Energy.

for the State to address with 1 Energy, unless that has already taken place and is a moot point.

The grant application process involved the direct participation of a former high level State Department of Commerce employee in a joint venture involving Sno PUD and 1 Energy, where funding was sought from and granted by the State Department of Commerce. The obligation to identify, address and resolve any issue under RCW 42.52.080 rested with 1 Energy and its employee.

However, any failure by 1 Energy or its employee to follow state law created potential risk for Sno PUD as the grant recipient. Paragraph 13 of the Clean Energy Fund Grant Agreement between the State Department of Commerce and Sno PUD states in relevant part:

Conflict of Interest. Notwithstanding any determination by the Executive Ethics Board or other tribunal, Commerce may, in its sole discretion, by written notice to the Contractor terminate this contract if it is found after due notice and examination by Commerce that there is a violation of the Ethics in Public Service Act, Chapter 42.52 RCW; or any similar statute involving Contractor in the procurement of, or performance under the contract.

Given the circumstances, the Utility should have requested 1 Energy to provide formal confirmation that all required steps had been taken to ensure 1 Energy's compliance with any pertinent State law or regulation.

XX. Mesa III - \$4 Million

Mesa III proposes a joint venture between Sno PUD, 1 Energy and Tesla. It calls for the fabrication of a prototype energy storage battery system with the battery to be designed and fabricated by Tesla to meet Mesa standards. 1 Energy would serve as the

systems integrator and provider of the software. 1 Energy brought the project proposal to the Utility.

There are substantial benefits that could accrue to the Utility if it proceeds with Mesa III. These are identified in the materials before the Commission.

The Commission will want to ensure that the proposed Mesa III contract would deliver sufficient value to the Utility to warrant proceeding. That requires identification and evaluation of what Tesla and 1 Energy offer to the Utility.

Like Mesa I and II, Mesa III is an R&D project. Presumably, Tesla has financial resources allocated to its own R&D budget. This raises the question whether the monies that would flow to Tesla under the Mesa III contract reflect the best economic deal for the Utility. Tesla will have the opportunity to establish a real-life, real-time prototype at a large operational Utility. If it succeeds, Tesla could be even better positioned in the lucrative power market, both nationally and globally.

As with the other Mesa projects, Mesa III is a special facilities contract. The approach was reportedly influenced in part by Tesla's desire to proceed quickly with the project. The optimal time table for the Utility may not align perfectly with Tesla's preferred timeline because of the Utility's established protocols for contract negotiations, drafting, review and approval. The problem for the Utility with a rushed process is that important steps can be omitted or unduly condensed. Tesla's timeline preferences may have already been fully evaluated and weighed by the Utility in the due diligence process that culminated in the waiver of the competitive procurement process for Mesa III.

The fact that Mesa I and II have not yet been fully completed further reinforces the need for a careful and thorough analysis of the Mesa III project.

XXI. Neither Steve Klein nor any Other Sno PUD Executive Received a Job Offer or Other Personal Financial Benefit

The Complaint suggests the possibility that the Mesa contracts might have been driven by a personal financial incentive. The Investigator found no evidence that Mr. Steve Klein sought or received a job offer from 1 Energy, or that he anticipated or received a financial stake in 1 Energy. (The same is true with respect to other Utility employees and executives.)

Based on Mr. Klein's own extensive resume and professional accomplishments, Mr. Klein would be an attractive hire to many prospective employers in this State and elsewhere.

Dated this 29th day of May, 2015.


Colleen Kinerk